

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
MERA DELICATESSEN, INC.	:	DETERMINATION
AND EMIL MEKHAIL, AS OFFICER	:	
for Revision of a Determination or for Refund	:	
of Sales and Use Taxes under Articles 28 and 29	:	
of the Tax Law for the Period September 1, 1982	:	
through February 28, 1985.	:	

Petitioners, Mera Delicatessen, Inc. and Emil Mekhail, as officer, 32-43 86th Street, Jackson Heights, New York 11369-2144, filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period September 1, 1982 through February 28, 1985 (File No. 802775).

A hearing was commenced before Dennis M. Galliher, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on June 9, 1987 at 1:45 P.M., was continued before Dennis M. Galliher, Administrative Law Judge, at the offices of the Division of Tax Appeals, Two World Trade Center, New York, New York, on December 8, 1987 at 1:15 P.M., and was continued to conclusion before the same Administrative Law Judge at the same location on December 6, 1988 at 1:15 P.M. Petitioners appeared on the first hearing date by Emil Mekhail, and on the two later hearing dates by Schneider and Tratner, Esqs. (Louis Tratner, Esq., of counsel). The Audit Division appeared at the first hearing date by John P. Dugan, Esq. (Michael Gitter, Esq., of counsel) and at the two later hearing dates by William F. Collins, Esq. (Michael Gitter, Esq., of counsel).

ISSUE

Whether the Audit Division properly determined upon audit that petitioner Mera Delicatessen, Inc. owed additional sales taxes, and that petitioner Emil Mekhail was responsible for the payment of such taxes pursuant to Tax Law §§ 1131(1) and 1133(a).

FINDINGS OF FACT

1. On November 14, 1985, the Audit Division issued two notices of determination and demands for payment of sales and use taxes due to petitioner Mera Delicatessen, Inc. ("Mera"), spanning, together, the period September 1, 1982 through February 28, 1985 and assessing a sales tax liability in the aggregate amount of \$79,767.02, plus penalty (Tax Law § 1145 former [a][1]) and interest. On the same date, the Audit Division issued two additional notices of determination and demands for payment of sales and use taxes due spanning the same period and assessing the same amounts as above, against petitioner Emil Mekhail as a person required to collect and remit taxes on behalf of Mera. These four notices were all based on the results of a field audit of the business operations of Mera as described hereinafter.

2. In or about November of 1984, the Audit Division determined to conduct a field audit of Mera's business operations. An auditor was assigned and an audit appointment letter scheduling an audit for November 19, 1984 was mailed to Mera. This appointment letter specified the audit period to be September 1, 1982 through August 31, 1984, and indicated that all records pertaining to Mera's sales tax liability should be available for review including, but not limited to, journals, ledgers, sales invoices, purchase invoices, cash register tapes, exemption certificates and any other sales tax records.

3. On August 27, 1984, prior to the issuance of the audit appointment letter, the auditor made an unannounced visit to the premises. The auditor observed the premises, located in Times Square (8th Avenue at 43rd Street), to consist of a coffee and sandwich shop selling coffee, rolls, sandwiches (ham, cheese, salami, tuna fish, etc.), cold cuts, beer, soda and other similar items. The auditor described the premises as relatively small in area, and also observed a sign attached to the door of the premises indicating the business was open 7 days per week, 24 hours per day. Petitioners purchased and commenced operation of this business in 1982. Prior to petitioners' purchase, a small delicatessen was operated at the premises. Petitioners initially paid \$1,200.00 per month to rent the premises, with such rent later increased to \$1,500.00 per month.

4. On the November 19, 1984 audit appointment date, the auditor went to the business premises. The only records made available to the auditor were certain bank statements, and a small portion of a cash receipts journal and a cash disbursements journal. There were no cash register tapes, guest checks, sales or purchase invoices, Federal income tax returns or withholding tax returns available.

5. Given the presentation of the limited records described above, the auditor concluded that Mera had inadequate books and records for purposes of conducting a detailed audit and therefore determined to resort to indirect audit methodologies. More specifically, the auditor conducted an observation of the premises on April 4, 1985 between the hours of 7:00 A.M. and 6:30 P.M. Although the business was allegedly open 24 hours per day, the business was closed abruptly at 6:30 P.M. on the day of the observation and the observation was, at that point, terminated. After such closing, the auditor visited other establishments in the area, questioned certain persons there, and was advised that Mera was open 24 hours per day, 7 days per week.

6. During the course of the observation the auditor totalled all sales made, including both taxable and nontaxable sales. The auditor recorded \$491.41 in taxable sales during the period from 7:00 A.M. to 6:30 P.M. Thereafter, the auditor doubled this amount of sales to account for the period spanning 7:00 P.M. to 7:00 A.M. In addition, the auditor observed delivery orders received by telephone at the premises. While no deliveries were made on the observation day due to illness of the delivery boy employed by Mera, the auditor assumed that on an ongoing basis delivery sales were made and thus added 10 percent (based upon prior audit experience) to the amount of sales observed to account for delivery sales. Accordingly, total taxable daily sales were determined to be \$1,081.10. The auditor then projected said amount over 7 days per week and 13 weeks per sales tax quarterly period (or 130 weeks in the 10 quarters covered by the notice of determination) to arrive at total taxable sales. The auditor compared this total to the total taxable sales reported per Mera's sales tax returns, and arrived at a \$966,873.00 increase over taxable sales reported, with additional tax due computed thereon in the amount of \$79,767.02. In turn, the notices of determination described in Finding of Fact "1" were issued to petitioners. The auditor recommended that penalty be assessed based primarily on the lack of records and the comparison of reported taxable sales by Mera (\$44.00 per day) versus taxable sales determined upon audit

(\$1,081.10 per day).¹

7. At hearing, petitioner Emil Mekhail admitted that he was a person required to collect and remit sales and use taxes on behalf of Mera during the period in question. However, petitioners contest the dollar amount of sales tax as determined upon audit.

8. Petitioner Emil Mekhail appeared and testified at hearing, and also presented some limited documentary evidence, including photographs of the premises and letters from some of Mera's suppliers reflecting dollar amounts of purchases by Mera during 1985.

SUMMARY OF PETITIONERS' POSITION

9. Mr. Mekhail asserts via testimony that Mera's markups over cost on the various items sold were extremely low and would not compare realistically to those necessary to support the audit results. Mr. Mekhail also testified, although without specificity, that for a short period of time the business was open 24 hours per day. However, because of crime problems in the neighborhood the business was allegedly closed between midnight and 6:00 A.M., with only an employee remaining inside the store at all times to avoid break-ins. Mr. Mekhail maintains that the Times Square area is busiest during the daylight hours through the time of approximately midnight. He testified that sales after midnight were virtually nonexistent, and therefore asserts the auditor's doubling of sales during the daytime observation period to account for sales during the nighttime period is inappropriate.

10. As noted, certain letters from some of Mera's suppliers spanning most of the year 1985 were submitted in evidence in support of the proposition that the purchases reflected thereon are insufficient to support sales and generate taxes in the amounts of the assessments issued herein. It was admitted that such was not a complete listing of all purchases from all suppliers, but rather reflect only those purchases which could be obtained. Petitioners further allege that construction and rehabilitation of various neighborhood buildings resulted in more construction workers in the area during the time of the audit observation than was the norm. In this vein, it is asserted that a greater number of people than usual would have come into the store on the day of the observation, thus resulting in sales on the observation date which were far in excess of sales ordinarily made by the business. Petitioners also noted that the observation date was at the beginning of the month (specifically on April 4), and that the area in which the business was located (Times Square) also housed several welfare hotels and a number of people receiving public support. Petitioners maintained that this support, in the form of monthly checks, was paid early in the month at which time the recipients had money and would be more likely to make purchases at the business as opposed to other times of the month. Petitioners thus assert that sales on the day of the observation may have been overstated based on this factor.

CONCLUSIONS OF LAW

A. Tax Law §§ 1135 and 1142.5 provide that a taxpayer is under a duty to maintain complete, adequate and accurate records of its sales and to make the same available for audit upon request. Tax Law § 1138 further provides that where adequate records are not maintained or

¹Gross sales reported by Mera for the entire period covered by the notices of determination totalled \$17,270.00.

made available, the Audit Division is entitled to resort to indirect methodologies, including external indices, in conducting audits and determining the accuracy of taxpayers' returns as filed.

B. It is undisputed that adequate and complete records as requested by the auditor were neither maintained nor available for the auditor to review. Conspicuously absent were guest checks, cash register tapes and complete sets of purchase or sales invoices, from which documents an audit trail could potentially have been established. Therefore, there is no question that it was entirely permissible for the Audit Division to resort to indirect audit methodologies in this case, including an observation of the premises and projections therefrom.

C. Petitioners have not presented evidence sufficient to either refute the audit methodology or allow reduction of the amount of tax or penalty determined to be due for the period under audit. As described in Paragraphs "9" and "10", petitioners offered a number of assertions with regard to the correctness of the audit results. However, none of these assertions were offered with specificity, nor were they presented with supporting documentation sufficient to allow any reasonably accurate determination or reduction to be arrived at therefrom. Standing out in particular as unexplained is why the business was abruptly closed at 6:30 P.M. on the day of the audit observation, in direct contradiction to Mr. Mekhail's testimony that the business was open until midnight (if not open for 24 hours). Even more difficult to comprehend is how petitioners could pay monthly rent of \$1,200.00, not to mention other expenses of operation, out of gross sales (revenues) of only \$17,270.00 as were reported for the entire 30 month period covered by the notices of determination (see ___ Findings of Fact "3" and "6"). It is clear that indirect audit methodologies may not always result in an exact determination of liability. It is equally clear that where a taxpayer's own failure to maintain adequate, accurate and complete books and records requires resort to such indirect audit techniques, exactness is not required of the Audit Division in arriving at its determination, and the consequences of recordkeeping failures in this regard weigh heavily against the taxpayer (Matter of Meskouris Brothers, Inc. v. Chu, 139 AD2d 813). Accordingly, the audit methodology employed herein and its results insofar as assessed for the period under audit are sustained.

D. Notwithstanding the foregoing, however, it is clear that the period covered by the notices of determination (9/1/82 through 2/28/85) (see ___ Finding of Fact "1") exceeds the period under audit for which records were requested (9/1/82 through 8/31/84) (see ___ Finding of Fact "2") by some six months. There is no evidence of any request for (or subsequent review of) records for any period after August 31, 1984. Rather, the results of the auditor's observation were extended to include the additional six-month period (9/1/84 through 2/28/85) covered in the assessments at issue. Such an extension of audit results beyond the actual period under audit for which records were requested (and reviewed) is impermissible (Matter of Ahmed S. Ahmed and Yahya Ahmed d/b/a A & A Grocery Store, Tax Appeals Tribunal, November 10, 1988; Matter of Anton's Car Care Center, Ltd., Tax Appeals Tribunal, November 23, 1988 [both citing Matter of Adamides v. Chu, 134 AD2d 776, lv denied 71 NY2d 806]). Accordingly, the amounts assessed for the last two quarterly periods per the notices of determination (9/1/84 through 2/28/85) must be cancelled.

E. The petition of Mera Delicatessen, Inc. and Emil Mekhail, as officer, is hereby granted to the extent indicated in Conclusion of Law "D", but is otherwise denied, and the notices of determination and demands for payment of sales and use taxes due dated November 14, 1985, as revised in accordance herewith, together with such penalty and interest as is lawfully due and owing, are sustained.

DATED: Albany, New York

February 9, 1989

Galliher _____ /s/ Dennis M.
ADMINISTRATIVE LAW JUDGE